

Message Text

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ACTION EUR-25

INFO OCT-01 EA-11 ADP-00 AID-20 CEA-02 CIAE-00 COME-00

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NSC-10 STR-08 PA-03 PRS-01 USIA-12 RSR-01 /177 W

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R 181739 Z MAY 73

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USEC BRUSSELS 7837

LIMITED OFFICIAL USE SECTION 1 OF 2 OECD PARIS 13859

E. O. 11652: N/A

TAGS: ECON, OECD, US

SUBJECT: EDRC REVIEW OF US ECONOMY, MAY 14

REF: EDR (73)8

1. SUMMARY. CHAIRMAN HERBERT STEIN OF CEA SAID US HAD NO RADICAL DIFFERENCES WITH SECRETARIAT' S VIEWS EXPRESSED REFD0C , BUT HE WAS INCLINED TO TAKE A MORE CONFIDENT VIEW OF US ECONOMY REDUCING ITS INFLATION RATE SIGNIFICANTLY WITH CURRENT FISCAL AND MONETARY POLICY. US HAS PASSED PEAK OF ACCELERATION AND POLICY STANCE IS TO DECELERATE ECONOMY GRADUALLY WITHOUT PITCHING IT INTO EXCESSIVE SLOWDOWN. STEIN SAID US HAD NO MAJOR DIS-AGREEMENT ON BALANCE OF PAYMENTS OUTLOOK BUT WAS PERHAPS LESS OPTIMISTIC THAN SECRETARIAT. END SUMMARY.

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2. PROSPECTS AND POLICIES: HERBERT STAIN, CHAIRMAN
CEA AND HEAD OF US DEL, SAID US HAD NO RADICAL DIFFERENCE WITH SECRETARIAT'S VIEWS ON US ECONOMY EXPRESSED REFDOC, BUT WOULD TAKE A MORE TWO UDED VIEW OF CURRENT SITUATION. HE SAID PEAK OF THE ACCELERATION HAD BEEN PASSED IN FIRST QUARTER 73 RESPECTING GROWTH GNP (NOMINAL AND REAL) AND PRICES. PRESENT RESTRICTIVE FISCAL AND MONETARY POLICIES WERE DESIGNED TO PREVENT EXCESSIVE BOOM WITHOUT PITCHING ECONOMY INTO EXCESSIVE SLOWDOWN AND SHOULD BE GIVEN MORE WEIGHT THAN SECRETARIAT ALLOWED. ESPANSION WAS BEING ALOWED DOWN BY RESTRAINT OF FEDERAL SPENDING AND BY RISING REVENUES (BUDGET DEFICITS FOR FISCAL 73 AND 74 WOULD BE REDUCED BY \$ 6 BILLION AND \$7 BILLION RESPECTIVELY), AND A RELATIVELY CONSTANT RATE OF GROWTH OF MONEY SUPPLY WOULD BECOME INCREASINGLY RESTRICTIVE AS ECONOMY CONTINUED TO GROW. THUS US EXPECTS A REAL SLOWDOWN IN THE GROWTH RATE OF BOTH GNP AND PRICES IN 1973 AND 1974, SOMEWHAT MORE THAN THE REVISED SECRETARIAT FIGURES, PARTICULARLY IN THE FIRST HALF 1974 , WHEN US EXPECTED 4 PER CENT REAL GROWTH RATE COMPARED TO SECRETARIAT'S 4.9.

3. PRICES AND WAGES: HE SAID
SECRETARIAT HAD OVER EMPHASIZED EFFECTS ON PRICES OF SHIFT FROM PHASE II TO PHASE III. THE BIG PRICE RISE IN FIRST QUARTER 1973 WAS ONLY PARTIALLY RELATED TO THE SHIFT. IN LARGE PART PRICE RISE WAS RELATED TO DEMAND PULL (HIGHLY CONCENTRATED IN FOOD AND A FEW INDUSTRIAL PRODUCTS), DEVELUA-TION AND A TEMPORARY IMPAIRMENT OF FOOD SUPPLIES. HE DISAGREED WITH SECRETARIAT'S VIEW ON FOOD PRICE DEVELOP-MENT FOR 1973 AND 1974. US AUTHORITIES EXPECTED LITTLE FURTHER RISE OF FOOD PRICES AT THE RETAIL LEVEL IN 1973. THESE DEVELOPMENTS WERE CONTINGENT ON WEATHER, (WHICH WOULD AFFECT MAINLY 1974 SUPPLIES) BUT WE EXPECT BIGGER SUPPLY FOOD IN 1973 THAN IN 1972. HE ALSO NOTED SECRETARIAT GIVES MORE IMPORTANT WEIGHT TO RISE IN INDUSTRIAL WHOLESALE PRICES THAN US DOES. HE REGARDED THESE RECENT RISES AS NON- RECURRING AND THEREFORE NOT A USEFUL PRECEDENT FOR ESTIMATING FUTURE PRICE DEVELOP-MENT IN US. IN THIS CONNECTION, STAIN SUGGESTED THAT LIMITED OFFICIAL USE

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USE OF FIRST QUARTER PRICE DATA AS EVIDENCE OF SHIFT IN TRADE- OFF BETWEEN UNEMPLOYMENT AND PRICE WAS HAZARDOUS BECAUSE OF THE LARGE NUMBER OF NON- RECURRENT FACTORS OCCURRING THEN. STEIN ALSO CITED THE GOOD PERFORMANCE WAGES IN 1972 AND GOOD BEHAVIOR OF COLLEC-TIVE WAGE AGREEMENTS THUS FAR THIS YEAR. HE NOTED LABOR LEADERS HAD TAKEN A POSITIVE ATTITUDE ON AGREEMENTE IN ORDER

TO AVOID IMPOSITION WAGE CONTROLS.

4. SECRETARIAT VIEWS: SECRETARIAT (ANDERSEN) ARGUED RISKS FOR US ECONOMY WERE OVERWHELMINGLY ON SIDE OF T O STRONG AN EXPANSION, WHICH WOULD BE FOLLOWED BY EXCESSIVE DOWNTURN. THE SECRETARIAT HAD ALSO BUILT IN SOME SLOWDOWN LATER IN 1973 AND 1974, BUT BIG QUESTION WAS HOW MUCH, GIVEN STRONG EXPANSIONARY FORCES, INCLUDING BUSINESS FIXED INVESTMENT N CONSTRUCTION ACTIVITY, AND STATE- LOCAL EXPENDITURE. APART FROM MARKED SLOWDOWN IN PRIVATE CONSUMPTION, WHICH ALREADY BUILT INTO SECRETARIAT DATA, ANDERSEN SAW NO IMPORTANT FORCES OPERATING TO SLOW DOWN ECONOMY SIGNIFICANTLY. HE SUGGESTED ANY ACTION DIFFI ULT TO TAKE, BUT IT WAS DESIRABLE US SHOULD MOVE IN FISCAL AREA; E. G., - 53.094-46 7 - PENSION OF INVESTMENT TAX CREDIT WOULD POSTPONE INVESTMENT TO NEXT YEAR WHEN IT WOULD BE MORE NEEDED.

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5. STEIN IN RESPONSE THIS VIEW, AS WELL AS TO MANY SIMILAR VIEWS EXPRESSED BY OTHER DELEGATIONS IN THEIR QUESTIONING, NOTED THAT MOST FORECASTS IN US SEE EVEN BIGGER SLOWDOWN THAN HE DOES. THERE WOULD BE A SWING OF OVER \$14 BILLION IN THE FULL EMPLOYMENT SURPLUS - A SIGNIFICANT CHANGE - AND CONGRESS ITSELF WAS AIMING AT A \$280 BILLION BUDGET FOR FY 1974. THE BEHAVIOR OF THE PRIVATE SECTOR WAS CAUTIOUS AND THERE HAD BEEN NO JUMP IN INVENTORY ACCUMULATION. POLICY WOULD NOT BE CHANGED UNLESS THERE IS CLEAR EVIDENCE OF NEED. STEIN EMPHASIZED LIMITED OFFICIAL USE
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THAT ADDITIONAL MEASURES COULD BE TAKEN IF WE CAME TO BELIEVE THEY ARE NECESSARY. HE INSISTED, HOWEVER, THAT THE PRESENT POLICY MIX IS APPROPRIATE TO BRING THE US ECONOMY ON THE PATH WANTED. FURTHER CUTS IN EXPENDITURES MIGHT BE POSSIBLE, BUT ONLY IN EXTREME SITUATION WOULD US AUTHORITIES LOOK TO THE REVENUE SIDE. WAGE STANDARDS WOULD BE ADMINISTERED FLEXIBLY, BUT LARGE PAY INCREASES WOULD BE STOPPED. AS TO THE USE OF THE TAX SURCHARGES OR REMOVAL INVESTMENT TAX CREDIT, STEIN DOUBTED, ON BASIS PAST PERFORMANCE, SUCH MEASURES WOULD PROVE EFFECTIVE.

6. BALANCE OF PAYMENTS: LEDERER (TREASURY) SAID US WAS MAKING PROGRESS TO CORRECT ITS BALANCE PAYMENTS DIS-EQUILIBRIUM. US MADE NO FORECASTS, BUT WE WOULD PER-HAPS BE A LITTLE LESS OPTIMISTIC THAN SECRETARIAT. ABSTRACTING FROM SPECIAL FACTORS THERE HAD BEEN ABOUT \$180 MILLION IMPROVEMENT IN THE TRADE BALANCE FROM THE FOURTH QUARTER 1972 TO THE FIRST QUARTER 1973. THIS PROBABLY REFLECTED, ON EXPORT SIDE, SOME ADJUSTMENT RESULTING FROM THE 1971 CHANGE IN EXCHANGE RATES AND PERHAPS CYCLICAL DEVELOPMENTS ELSEWHERE. NO NET EFFECT OF CHANGE IN EXCHANGE RATES ON IMPORTS WAS EVIDENT, ALTHOUGH THESE COULD HAVE BEEN HIDDEN BY CYCLICAL DEVELOPMENT IN THE US. HE THOUGHT AGRICULTURE EXPORTS HAD PEAKED IN FIRST QUARTER 1973 AND THAT THEY WOULD DECLINE IN THE LATER HALF THIS YEAR AND MAYBE INTO 1974. AGRICULTURAL EXPORTS MIGHT AMOUNT TO \$13.5 BILLION IN 1973. FUEL IMPORTS WOULD CONTINUE TO RISE BUT PERHAPS NOT SO STRONGLY AS EARLIER THIS YEAR. AS TO EFFECT 2 ND DEVELUATION OF DOLLAR, LEDERER SAID WE WOULD HAVE TO WAIT TO SEE WHETHER HIGHER PRICES FOR IMPORTS WILL DISCOURAGE THEM. PROBLEM IS THAT FOR MANY COMMODITIES WE HAVE NO DOMESTIC SUBSTITUTES, AND THE PROCESS OF DECISION MAKING TO INVEST AND TO BRING ON STREAM IMPORT SUB-

STITUTE PRODUCTS TAKES TIME- PERHAPS A YEAR OR MORE.
HE ALSO COMMENTED ON LARGE INTEREST PAYMENTS TO
FOREIGN HOLDERS OF US SHORT TERM ASSETS AND LARGE
CAPITAL INFLOWS INTO US STOCK MARKET (\$4 BILLION AN.
RATE IN LAST 6 MONTHS). HE EXPECTED FOREIGNERS TO
CONTINUE BUY LARGE AMOUNTS US STOCKS.

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7. MEDIUM TERM ISSUES: STEIN DISCUSSED THE ADMINISTRA-
TION' S PROGRAM TO DECENTRALIZE MANPOWER PRGRAMS. HE
NOTED FULL EMPLOYMENT COULD NOT BE DEFINIED BY ANY
STATISTIC IN ADVANCE, AND GENERAL PHILOSOPHY OF THE
ADMINISTRATION IS TO CREATE CONDITIONS IN WHICH THE
ONE WHO SEEKS WORK REALISTICALLY ON REASONABLE TERMS
CAN FIND IT. THE MOST IMPORTANT THING THE GOVERN-
MENT CAN DO IS TO MAINTAIN THE STEADY GROWTH OF THE ECONOMY.
HE SAID HE WAS UNCERTAIN HOW WELFARE MAY OPERATE THIS WAY
FOR OLDER PEOPLE. THE MINIMUM WAGE MAY ACT AS A DISINCENTIVE
TO HIRING THE YOUNG, AND THE ADMINISTRATION WAS TRYING TO GET
A DIFFERENTIAL FOR THEM. HE NOTED THAT ONE SHOULD LOOK WITH
CAUTION AT THE HIGH FIGURES FOR YOUTH UNEMPLOYMENT . YOUNG
PEOPLE IN THE US TEND TO SHIFT AROUND TRYING DIFFERENT
JOB OPPORTUNITIES. UNLIKE THEIR EUROPEAN COUNTERPARTS
WHO SETTLE INTO AN APPRENTICE SYSTEM. MANY ARE ALSO
STUDENTS SEEKING PART- TIME WORK, AGAIN DIFFERENT FROM
THE EUROPEAN SCENC. THE UNEMPLOYMENT PROBLEM FOR WOMEN
WORKED RELATIVELY LITTLE HARDSHIP ON THEM, AND THE PROBLEM
WAS LESS THAN FOR YOUTH. THERE ARE ALSO PERSISTENT
DIFFERENCES IN CERTAIN REGIONAL AND SECTORAL UNEMPLOYMENT
RATES BUT THESE WERE NOT DISEQUILIBRIUM RATES. REGIONAL
UNEMPLOYMENT RATES HAD BEEN NARROWED AND US IS NO LONGER
OBSESSED WITH REGIONAL PROBLEMS. HE AGREED WITH THE
SECRETARIAT' S VIEW THAT US EMPLOYME
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